In the Supreme Court of the United States

OCTOBER TERM, 1965

No. 351

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

WALTER F. TELLIER AND EVELYN H. TELLIER

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF FOR THE PETITIONER

1. Respondent challenges (Br. 8–20) the government's statement that the Commissioner's position in the instant case is supported by 40 years of uniform administrative practice and judicial decisions. Respondent concedes that from 1924 to 1944 and, again, from 1956 on the Commissioner and the courts consistently disallowed deductions such as those here in question. Respondent argues, however, that in 1944 both the Commissioner and the Tax Court abandoned their earlier position and that it was not until 1956 that they reinstated their earlier policy of disallowing such expenses. His claim is that *Longhorn Portland Cement Co.* v. *Commissioner,* 3 T.C. 310 (1944) and G.C.M. 24377, 1944 Cum. Bull. 93, show that the

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Tax Court and the Commissioner "abandoned" their prior consistent policy of disallowance (Br. 12). We disagree.

It is clear that neither *Longhorn* nor G.C.M. 24377 constituted a reversal of the well established general rule of non-deductibility. At most they represented a very limited exception to the general rule—one relating only to the expenses of defending against an antitrust prosecution.[1] The limited antitrust exception was revoked by the Commissioner in 1962. Rev. Rul. 62–175, 1962–2 Cum. Bull. 50. It is manifest from the many cases decided between 1944 and 1956 that, with the sole exception of antitrust suits, the general rule of non-deductibility was consistently applied.

In 1945—one year after respondent claims that the Commissioner and the Tax Court had "abandoned" the general rule of non-deductibility—the Tax Court decided *Greene Motor Co.* v. *Commissioner,* 5 T.C. 314. While the court allowed the disputed deduction, it did so only because the attorney's fees there in question were incurred in arranging a settlement of potential civil and criminal liabilities. In reaching this result, the court recognized that such expenses would have been non-deductible if "the defense was unsuccessful and conviction followed" (p. 319). The court thought this general rule so well-established that "Citation of such cases is considered

[1] In fact, *Longhorn* related to an antitrust suit brought by the State of Texas which had been settled without conviction. Thus only G.C.M. 24377 concerned expenses of unsuccessfully defending an antitrust prosecution.

unnecessary here" (*ibid.*). However, the court declined to apply the rule where there had been "compromise" instead of "conviction" (p. 320, 321, 322).

Two years later in *Stralla* v. *Commissioner,* 9 T.C. 801, 821 (1947), the court specifically denied a deduction for attorney's fees connected with the unlawful operation of a gambling ship on the ground that "allowance of the deductions here claimed would * * * frustrate sharply defined * * * [State] policies." See, also, *Thomas* v. *Commissioner,* 16 T.C. 1417 (1951), and *Schwartz* v. *Commissioner,* 22 T.C. 717 (1054), affirmed, 232 F. 2d 94 (C.A. 5).[2]

Respondent cites (Br. 11, 12) the case of *Joseph* v. *Commissioner,* 26 T.C. 562 (1956) and Rev. Rul. 62–175, 1962–2 Cum. Bull. 50, as marking the "revival" by the Tax Court and the Commissioner of the general rule disallowing fees incurred in unsuccessfully defending a criminal prosecution. As the Tax Court's opinion in that case discloses, the *Joseph* case is merely one of the unbroken line of cases, both before and after 1944, applying the general rule of non-deductibility. The Tax Court opened its *Joseph* opinion with the statement that (p. 564) "We have held in a number of cases beginning as early as *Sarah Backer,* 1 B.T.A. 214 [1924], that legal expenses in-

[2] *Thomas* explicitly disallowed "attorneys' fees paid * * * in the unsuccessful defense of a criminal indictment." In *Schwartz* the court allowed a deduction for certain legal fees which had no connection with the criminal prosecution and noted that the taxpayer was not even claiming a deduction "for the fees of the attorney who handled the criminal trial" (22 T.C. at 721).

curred in the unsuccessful defense of a criminal prosecution are not deductible."

2. As explained in our opening brief, while the lower courts have disallowed deductions like those here in question on three grounds, the Commissioner is now placing reliance only on the public policy ground. Respondent answers (Br. 12) that since this Court's 1943 decision in *Commissioner* v. *Heininger,* 320 U.S. 467, "no court" has supported disallowance of attorney's fees on grounds of "overriding public policy." This is plainly incorrect.

In *Thomas* v. *Commissioner,* 16 T.C. 1417 (1951), the court explicitly denied a deduction for attorney's fees because, *inter alia,* "allowance of a deduction would be against public policy" (p. 1418). And in *Stralla* v. *Commissioner,* 9 T.C. 801 (1947), the court stated that "allowance of the deductions [for attorneys' fees] here claimed would be in our opinion 'to frustrate sharply defined * * * [State] policies'" (p. 821).[5]

Nor have the courts of appeals ceased to rely upon that ground. In the recent case of *Bell* v. *Commissioner,* 320 F. 2d 953, 956 (C.A. 8 1963), the court denied a deduction for attorneys' fees incurred in connection with taxpayer's criminal conviction, stating that one of the "[g]rounds for denial of deductibility

[5] As explained *supra* pp. 2–3, the court in *Greene Motor Co.* v. *Commissioner,* 5 T.C. 314 (1945), allowed a deduction for attorneys' fees only because they were incurred in connection with a "compromise" of potential civil and criminal liabilities rather than a "conviction," and thus, allowing a tax deduction would "involve no frustration of any public policy."

[is] * * * that to allow as a deduction the expenses incurred in unsuccessfully defending a criminal prosecution would violate public policy." Other recent appellate decisions dealing with attorneys' fees state the general rule of non-deductibility and cite in support cases expressly resting on considerations of public policy. See, *e.g., Port* v. *United States,* 163 F. Supp. 645, 647 (Ct. Cl. 1958), and *Hopkins* v. *Commissioner,* 271 F. 2d 166, 167–168 (C.A. 6 1959), citing *Burroughs Building Material Co.* v. *Commissioner,* 47 F. 2d 178, 180 (C.A. 2) (such fees disallowed "on grounds of public policy"), and *Thomas* v. *Commissioner,* 16 T.C. 1417, 1418 ("The allowance of a deduction [for such fees] would be against public policy."). See also *Jerry Rossman Corp* v. *Commissioner,* 175 F. 2d 711, 713 (C.A. 2 1949).

Respectfully submitted.

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